No. 97-2063

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October Term, 1997

STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY,

Petitioner,

against

THE HONORABLE JOHN SPERONI,
TAMMY SNIDER and MICHAEL AVERY,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
ILLINOIS SUPREME COURT

BRIEF OF THE STATE OF NEW YORK AS *AMICUS CURIAE* IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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INTEREST OF *AMICUS CURIAE*

The State of New York submits this brief *amicus curiae* in support of the petition for a writ of certiorari by State Farm Mutual Automobile Insurance Company. New York objects to the judgment of the Illinois Supreme Court leaving intact the Illinois Circuit Court's grant of plaintiffs' motion to certify a nationwide class of approximately 5,000,000 insurance policyholders in 48 states in litigation raising, among other things, consumer fraud claims to be governed by Illinois law.

New York has a significant interest in having this Court review the decision to certify a nationwide class in this matter.

State Farm is the largest auto insurer in the United States, providing automobile insurance coverage to one out of every five insured drivers nationwide. State Farm insures close to 13.1% of the New York private passenger auto market, making it the second largest automobile insurer in the State. Approximately 1.24 million automobile physical damage policies are written by State Farm each year for New York residents, generating approximately $324 million in insurance premiums. Roughly 40% to 50% percent of the premiums charged in New York for comprehensive and collision coverage is attributable to coverage for physical damage to vehicles, which includes the coverage for replacement parts.

The claims in this case concern State Farm's practice of using nonoriginal equipment manufacturer ("non-OEM") replacement parts in the repair estimates for damaged automobiles, where the non-OEM parts are priced lower than original equipment manufacturer ("OEM") parts.The several states have adopted varying regulations with regard to the use of non-OEM parts. Some states, as in New York, permit and indeed encourage the use of these parts, while other states require their use. *See Petition*, n.7.

The Illinois court has ruled that the issue of whether State Farm's policy of using non-OEM parts constitutes a violation of the Illinois Consumer Fraud and Deceptive Business Practices Act is appropriate for class resolution. The order of class certification will thus result in the application of Illinois law to the claims of New York policyholders, as well as those of 47 other states, all of whom contracted with State Farm subject to the various regulations of those separate states. This raises the significant question of whether a state is protected against the extraterritorial application of another state's law in possible contravention of its own regulatory preferences, and of the sovereign right of each state to regulate the business of insurance within its own geographical boundaries.

SUMMARY OF ARGUMENT

Allowing this matter to proceed as a nationwide class action sets up a very real potential for conflict between the extraterritorial application of Illinois law and each state's own regulatory scheme to the detriment of the sovereign right of every state to regulate the business of insurance within its borders. Moreover, given the ever-present possibility of settlement in a nationwide class action, the Court may never have any other opportunity to review this order, which could directly intrude upon and undermine the several states' ability to implement their own regulatory choices.

ARGUMENT

I

PERMITTING THIS NATIONWIDE CLASS ACTION TO PROCEED WOULD ALLOW THE COURT OF ONE STATE TO OVERRIDE THE POLICIES AND REGULATIONS OF OTHER STATES AND SEVERELY IMPEDE THE ABILITY OF THE INDIVIDUAL STATES TO REGULATE THE BUSINESS OF INSURANCE

The United States Constitution has as one of its fundamental precepts a respect for the sovereignty of the individual states. As this Court long ago explained:

> The several States are of equal dignity and authority, and the independence of one implies the exclusion of power from all others. And so it is laid down by jurists, as an elementary principle, that the laws of one State have no operation outside of its territory, except so far as is allowed by comity; and that no

> tribunal established by it can extend its process beyond that territory so as to subject either persons or property to its decisions.

Pennoyer v. Neff, 95 U.S. 714, 720-722 (1877).

This principle of state sovereignty is embodied not only in the federal Constitution but in federal legislation as well. Its relevance here is most apparent in the McCarran-Ferguson Act of 1945, 15 U.S.C. § 1011 *et seq.*, where Congress declared that "the business of insurance, and every person engaged therein, shall be subject to the laws of the several states," 15 U.S.C. § 1012(a), thereby emphasizing the primacy of state regulation of insurance. *See generally United States Dep't of Treasury v. Fabe*, 508 U.S. 491, 500 (1993).

In ruling that this action may be maintained as a class action, the Illinois court determined that the question of whether State Farm's practice of using non-OEM parts constitutes a violation of the Illinois Consumer Fraud and Deceptive Business Practices Act is a common issue appropriate for class resolution under Illinois law. *Petition*, App. 9a. If this determination is permitted to stand, a single state court could effectively disrupt the entire system of individual state insurance regulation, contrary to the McCarran-Ferguson Act and the underlying constitutional precepts of individual state sovereignty.

The State of New York has a carefully calibrated regulatory scheme setting forth "standards for prompt, fair and equitable settlement of motor vehicle physical damage claims." 11 NYCRR § 216.7. That regulatory scheme, based, *inter alia*, on a policy of cost control, allows an insurer's repair estimate to be

based upon the use of nonoriginal equipment manufacturer crash parts[1], as follows:

> (5) If the insurer's repair estimate is based upon the use of any non-OEM crash part:
>
> (i) the estimate shall specify the non-OEM or non-OEM supplier;
>
> (ii) the insurer shall not, without consent of the insured or the insured's designated representative, specify non-OEM crash parts from more than three different suppliers for any one repair;
>
> (iii) the crash part shall equal or exceed the comparable OEM crash part in terms of fit, form, finish, quality and performance;

---

[1]The regulation defines "crash part" to mean "a part of a motor vehicle, which (i) is made of sheet metal, plastic, fiberglass, or similar material, including a door, fender, panel, bumper, hood, floor or trunk lid, but not including windows or hubcaps; and (ii) constitutes or provides support for the motor vehicle's exterior." 11 NYCRR § 216.7(a)(6). "Original equipment manufacturer" or "OEM" is defined to mean "a motor vehicle manufacturer or distributor that produces or markets, under its own name, crash parts for use in motor vehicles that it manufactures or distributes under its own name." 11 NYCRR § 216.7(a)(7). "Nonoriginal equipment manufacturer" or "non-OEM" means "a manufacturer or distributor (including any entity supplying the required warranty other than a manufacturer), that produces or markets, under its own name, crash parts for use in motor vehicles that it does not manufacture or distribute." 11 NYCRR § 216.7(a)(8).

(iv) the crash part must be warranted by the non-OEM at least to the extent and duration as the comparable OEM crash part;

(v) the insurer shall specify only certified crash parts, in regard to any part that has been duly certified by a qualified certifying entity acceptable to the superintendent;

(vi) if the crash part has not been certified by a qualified certifying entity acceptable to the superintendent, the non-OEM must issue a written warranty, for at least the period of the insured's ownership of the vehicle, that the crash part equals or exceeds the comparable OEM crash part in terms of fit, form, finish, quality and performance; and

(vii) the insurer shall cause the damaged vehicle to be restored to its preloss condition consistent with the non-OEM warranty, at no additional cost to the insured and within a reasonable time, if the non-OEM fails to honor its warranty required in subparagraph (iv) or (vi) of this paragraph.

11 NYCRR § 216.7(b)(5).

This regulatory provision is designed to balance consumer interests by permitting competition to operate in the pricing of repair parts while assuring that only quality and warranted parts will be used in repair estimates. Consumer cost containment is the primary goal.

The certification of a nationwide class action in which the claims of all State Farm policyholders are to be adjudicated based on Illinois law sets up the very real potential for conflict between the extraterritorial application of the Illinois statute and New York's carefully crafted regulatory scheme governing its insurance industry. If State Farm's policy on use of non-OEM

parts is found to violate the Illinois consumer fraud statute as applied to a national class, it can be anticipated that not only State Farm but all insurers will immediately change their claims handling practices to specify the use of only original equipment crash parts in repair estimates to avoid statutory liability. This would directly intrude upon and undermine New York's ability to implement its policy of cost containment as articulated in the aforestated regulation.

Allowing an Illinois court to apply its own law to override the regulatory choices of the various states would certainly be contrary to the spirit, if not the letter of the McCarran-Ferguson Act. *See F.T.C. v. Travelers Health Assn.*, 362 U.S. 293, 300-302 (1960) (noting that it would be inconsistent with the purposes of the Act to "delegat[e] to any one State sole legislative and administrative control of the practices of an insurance business affecting the residents of every other State in the Union"). The application of the Illinois law here could effectively sweep aside the multiple and distinct policy reasons for each state's own regulatory structure. Such an override of state policy and regulation could occur in every state in which a member of the class resides -- a total of 48 states in all. Moreover, it would likely lead to the situation in which State Farm is required under the laws and regulations of one state to specify the use of non-OEM parts while being held liable for doing so under the laws of another. *See Petition*, n.7.

The nationwide class certification threatens these results on the slender justification of facilitating litigation and preserving scarce judicial resources both in Illinois and other states. *Petition*, App. 6a. While these are laudable goals, they are insufficient to overcome principles of state sovereignty and comity to allow a state to "legislate" beyond its borders. *See BMW of North America v. Gore*, 517 U.S. 559, 568-69, 572-73 (1996) ("No one doubts that a State may protect its citizens by prohibiting deceptive trade practices...But the States need not,

and in fact do not, provide such protections in a uniform manner....Alabama may insist that BMW adhere to a particular disclosure policy in that State. Alabama does not have the power, however, to punish BMW for conduct that was lawful where it occurred and that had no impact on Alabama or its residents. Nor may Alabama impose sanctions on BMW in order to deter conduct that is lawful in other jurisdictions.").

II

IMMEDIATE REVIEW IS REQUIRED IN ORDER TO PREVENT THE COMPROMISE OF NEW YORK'S ABILITY TO REGULATE THE BUSINESS OF INSURANCE EFFECTIVELY.

Review of the order of class certification at this stage of the litigation is necessary in order to avoid the immediate potential for conflict among the several states. If settlement occurs, an order which impermissibly calls for the extraterritorial application of Illinois law will never be reviewed. Indeed, whether or not settlement occurs here, the order of class certification immediately impacts New York's sovereign right freely to regulate its own insurance industry, by creating the potential that the law of another state may be deemed applicable, in any class action, to the conduct of the insurance business in this State. New York has every interest in protecting its insurance laws, regulations, and policies against such a compromise.

CONCLUSION

For the foregoing reasons, New York, as *amicus curiae*, respectfully urges the Court to grant the petition for a writ of certiorari.

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August 21, 1998

Respectfully submitted,

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